2844

HOSPITAL SERVICE ASSOCIATION—§§1739.01 to 1739.15 R.C.—GROUP CONTRACTS; PARTIES TO SUCH CONTRACTS; PREMIUMS BASED ON SUCH GROUPS.

SYLLABUS:

A hospital service association organized under Sections 1739.01 to 1739.15, Revised Code, may enter into group contracts so that the association is one contracting party and a "group," as a unit, the other contracting party, and that a hospital service association may base the fees it charges individuals on the hospitalization experience of the group to which the individual belongs.

Columbus, Ohio, October 6, 1958

Hon. Arthur I. Vorys, Superintendent of Insurance
Department of Insurance, Columbus 15, Ohio

Dear Sir:

I have before me your communication regarding the authority of hospital service associations organized under Sections 1739.01 to 1739.15, Revised Code. Your specific questions are, to quote from your letter:

> "1. Under present practices the hospital service associations have contracts with the individuals even in those cases where the individuals are employees of a common employer; that is to say,

each contract is between the corporation and the individual subscriber. May hospital service associations enter into 'group' contracts so that the association would be one contracting party and a 'group' the other contracting party rather than the association entering into a number of individual contracts with the members of a 'group'?

"2. May hospital service associations enter into contracts with the individuals comprising a group as distinguished from a contract with the group, and base the fees charged each individual on the hospitalization experience of the group?"

The hospital service associations are non-profit corporations and their authority is set out in paragraph (A) of Section 1739.01, Revised Code.

"(A) 'Hospital service association' means any corporation organized not for profit under sections 1702.01 to 1702.58, inclusive, of the Revised Code, for the *purpose of establishing, maintaining, and operating a nonprofit hospital service plan* by which hospital care may be provided by a nonprofit hospital, or by a group of such hospitals, with which such corporation has a contract for such purpose, to such of the public as become subscribers to said plan under a contract which entitles each subscriber to hospital care. (Emphasis added)

The business of insurance has been highly regulated by the state and the legislature has in many instances specifically spelled out detailed provisions concerning the terms of insurance contracts and the type of contracts that can be written. Hospital service associations are engaged in a business substantially amounting to insurance, *Cleveland Hospital Service Assn.* v. *Ebright,* 142 Ohio St., 51; however, they are specifically exempt from the insurance laws—Section 1739.02, Revised Code.

Special regulation of hospital service associations has been relatively recent although the existence of such organizations has long been recognized in the statutes. The first mention of them is in 97 Ohio Laws, 287 (1904), where they are exempt from the insurance laws:

"* * * provided that nothing in this chapter, or in any other statute of the state of Ohio pertaining to insurance, shall so operate or be construed as to apply to the establishment and maintenance by individuals, associations or corporations, of sanatoriums or hospitals for the reception and care of patients for the medical, surgical or hygienic treatment of any and all diseases, or for the instruction of nurses in the care and treatment of diseases and in hygiene, or for any and all said purposes, *nor to the furnishing of any or all of said services, care or instruction in or in connec-*

> *tion with any such institution, under or by virtue of any contract made for such purposes,* with residence of the county in which such sanatorium or hospital is located." (Emphasis added)

It should be noted the care could be provided by "any contract." This provision in the law was carried in the General Code under the Chapter 2, Superintendent of Insurance, Section 669, and a predecessor of mine was called upon for an opinion on it and while the opinion is only of historical interest it is worthwhile noting that contracts for furnishing hospital service to "the general public individuals or groups" were held exempt, Opinion No. 1630, Opinions of the Attorney General for 1933, p. 1484. The syllabus of that opinion is as follows:

> "By virtue of the provisions of section 669 of the General Code, none of the laws of this state regulating or pertaining to insurance applies to contracts for the furnishing of hospital service to the general public, individuals or groups, for a certain stipulated charge per year, so long as such contracts are made only with persons for whom such service is to be rendered who are residents of the county where the hospitals ar sanatoriums in which such service is to be furnished are located."

Special provisions as to nonprofit corporations which had been or would be organized under the general corporation act were not enacted until 1939, 118 Ohio Laws, 154. This 1939 law is essentially the same as the law today.

In determining the answer to your first question, we must look to the rules for determining the extent and nature of corporate powers. The tendency has been for courts to liberally construe such powers.

> "* * * 'The modern doctrine is, to consider corporations as not only having such powers as are specially granted by the act of incorporation, but such as are necessary for the purpose of carrying into effect the powers expressly granted. * * * a power granted to a corporation, to engage in a certain business, carries with it the authority to act, * * * in carrying on such business, and * * * it would possess for this purpose the usual and ordinary means of accomplishing the objects of its creation in the same manner, as though it were a natural person.' * * *" 12 Ohio Jurisprudence, Corporations, Section 273, p. 347.

> "Private corporations are not restricted to the exercise of powers expressly conferred up on them, but have certain well-recognized and implied powers which are necessary to carry out powers expressly granted. These implied powers, moreover, are

> not limited to such as are indispensably necessary for the purpose of carrying into effect the powers granted, or to accomplish the purposes for which the corporations were created, but include those that are necessary in the sense of being appropriate, suitable, and convenient, including the right of reasonable choice of the means to be employed. * * *" 13 Ohio Jurisprudence, Corporations, Section 970, Pages 464, 465.

The purpose of a hospital service association is to establish, maintain and operate a nonprofit hospital service plan, and such corporations have expressed and implied powers to do those things necessary to accomplish that purpose.

There is little in the code which describes the requisites of a hospital service plan. There must, however, be two types of contracts, one with the hospital which provides the care, and the other a contract which entitles each subscriber to the hospital care. There is no provision in the code requiring the contract be made with the person that goes to the hospital. The only requirement is that the care must be provided under a contract entitling each subscriber to that care. A contract made between the association and an employer for the care of employees would meet this requirement. That is, it would be a contract entitling each subscriber to hospital care.

The insurance laws regulate certain types of "group" insurance contracts and they specifically set out what is necessary before such contracts can be made and prohibit any "group" contracts which are not in conformity with those requirements in Section 3917.01, Revised Code (group life insurance). The legislature therefore, when it desires to restrict or prohibit "group" contracts, can do so and has done so, but in the case of hospital service associations no such limitations were placed upon their authority or powers, so that no such restriction must have been intended.

A question has been raised as to the authority of the associations to enter into "group" contracts because of the use of the term "subscriber" in the code and the suggestion is that from reading all the sections relating to hospital service associations the conclusion is that only contracts between the association and individuals are authorized.

Certain sections of the code refer to the contracts "between such association and the subscribers * * *," as in Section 1739.05 (F)(2), Revised Code; or to contracts "issued by such association to the subscribers * * *," as in Section 1739.06, Revised Code; and to "a contract which entitles each subscriber to hospital care," as in Section 1739.01(A), Revised Code.

The word subscriber is not defined in the code and its use does present some difficulty. However, even under the presently operated hospital service plans a contract which entitles each subscriber to hospital care has not been construed to mean that only the person with whom the association contracts is entitled to the care. The family of the person is often entitled to hospital care. Under these contracts "subscriber" is sometimes defined to mean the contract holder, his or her spouse and their children within certain age brackets.

Such contracts which cover a family are group contracts. In 1940 the then attorney general was ruling on so-called "family policies" of life insurance, and the provision in the code that it was unlawful to make a contract of life insurance covering a group except as provided for in the code:

> "It has been suggested that the word 'group' as used in the quoted portion of Section 9426-2, General Code, applies only to employee groups and has no applicability to family groups, and that the prohibition contained in this section relates only to group life insurance as defined by the Act and does not include family groups. However, there is nothing in the language used by the General Assembly to indicate that there was any such legislative intention, and I know of no principle of statutory construction which would justify restricting or limiting the meaning of the word 'group' as used in Section 9426-2, General Code, to employee groups.
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> "The General Assembly has absolutely prohibited the making of any contract of insurance in this State covering a group, except as provided in the Group Life Insurance Law. In the form of policy submitted, it is proposed to insure several members of a family, and it therefore falls within the scope of the prohibition contained in the language quoted from Section 9426-2, General Code." Opinion No. 2729. Opinions of the Attorney General for 1940, P. 838 at 841.

As the hospital service plans are now operated the word "subscriber" has a very broad meaning but even if the ordinary dictionary meaning is given to the word it is consistent with the authority of the associations to make "group" contracts. The employer who contracts with the association would be the person who would sign or agree to the group contract and would be a "subscriber." The term subscriber is defined in Webster's New International Dictionary, Second Edition, page 2513, as:

> "One who subscribes; specifically: (a) one who signs, as a letter, document, agreement, etc. (b) One who agrees or consents, * * *."

While the subscriber may the one *entitled* to the hospital care there is no requirement that he must be the one who personally receives it, that is, the subscriber may be entitled to have the care given to someone else, just as the contract holder under the present hospital service contracts may be entitled to have the hospital care given his children. The use of the word "subscriber" is not inconsistent with the authority of hospital service associations entering into "group" contracts.

In response to question number two, it is commonly known that insurance companies, whether they are a life, fire or casualty company, charge differing rates for insurance. That is to say, a person sixty years old would ordinarily pay a higher rate for his life insurance than a person twenty years old, and the fire insurance rate for a frame house would ordinarily be higher than the rate for a similar brick house.

The purpose and reason for establishing "classes" for setting rates is sent out in Mehr and Cammack, *Principles of Insurance,* pp. 586, 587 and 588:

> "Rate making involves adherence to a number of fundamental principles. Rates must be adequate, equitable, not excessive, economically feasible, stable, and flexible, and should encourage loss prevention. * * *
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> "At first glance, it would seem that, as far as the company is concerned, adequacy of rates alone wuld be a sufficient criterion. But this is not true. It is also important to both insured and insurer to have equitable rates. Equity in rate making means the fixing of rates in such a way that each policyholder pays his fair share of the risk assumed by the insurance company.
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> "Although equity is easy to define in the abstract, it is impossible to obtain in practice. Indeed, perfect equity is unrealistic. To achieve it, each insured would have to be placed in a special category all by himself, for no two insureds present exactly the same conditions of risk. If each insured were put into a separate category, the whole principle of insurance—statistical prediction of total loss values through study of large numbers of homogeneous units—would be thrown overboard. So in insurance, at least, complete equity is a contradiction.
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> "* * *
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> "A practical degree of equity is obtained, however, by the pooling of similar risks into classes. But the degree of similarity among risks in a given class may vary a great deal. In fire insurance rating, for example, virtually all frame residences with a fire-resistant roof in a given town may have the same fire rate. This

> certainly does not mean that there is no variation among frame houses as to their likeliehood of burning. It would be too big and expensive a job, however, further to classify houses to get a higher degree of equity. To do so, the rates for all types of houses would have to be increased to cover the extra cost of inspection and rating. Further difficulty would be encountered in that additional classifications of houses for rating purposes might produce rate classes with so few members in them that the basic principle of the pooling of risk would be violated: The number of exposure units would be too small to allow the prediction of losses."

While your second question uses the term "group", actually it would seem that the proposal is to establish something in the nature of a classification of risks. The class in this case being based on employment. There would be a different rate for the different class. The rates charged for hospital service contracts are required to be "fair and reasonable" or "lawful, fair and reasonable" to the satisfaction of the superintendent of insurance, Section 1739.05, Revised Code. I find no other restrictions concerning the rates or fees charged by hospital service associations.

There are no specific provisions in the hospital service association sections of the code for establishing different classes for rate purposes, but there are also no provisions prohibiting using different classes so long as any classification results in rates that are fair and reasonable. Classification of risks is a common and customary insurance practice. As pointed out earlier, hospital service associations are making contracts which substantially amount to insurance and such associations having the power to make such contracts have at least an implied power to make classifications of such contracts for rates or fee purposes.

As a matter of fact, the hospital service associations are now and have been classifying their subscribers and charging different rates depending upon whether they are "payroll deduction subscribers" or "direct pay subscribers," and I understand that the difference in rate is based not only on a difference in premium collection costs but also is based on the utilization of the two different classes. I also understand that these rates have been approved by the Department of Insurance.

Insurance companies are not free from regulation in establishing their classifications for rates. They cannot act arbitrarily among other restrictions, the fire and casualty rates must not be unfairly discriminatory, Sections 3935.03 and 3937.02(D), Revised Code, and unfair discrimination

among individuals of the same class is prohibited in life insurance rates, Section 3901.21(F), Revised Code.

As mentioned before, the rates charged by hospital service associations must be "lawful, fair and reasonable." If a rate is unfairly discriminatory it would not be lawful, fair and reasonable, and your request indicates concern that the suggested method of establishing a rate might be unfairly discriminatory.

A 1946 Attorney General's opinion discussed the provision in the law prohibiting life insurance companies from unfairly discriminating between insureds of the same class in the amounts of premium charged. One rate, a lower one, was charged to persons under a salary deduction plan, and another rate to persons not under the plan. The opinion says that if there is a reasonable basis for a difference between the two groups then they are not in the same class, or, stated another way, the two rates do not cause an unfair discrimination. While the opinion speaks in terms of "class" the same logic would apply to determining whether a rate was unfairly discriminatory and thus not "lawful, fair and reasonable."

The opinion quotes from a report from the Attorney General of Florida, Opinion No. 965, Opinions of the Attorney General for 1946, p. 361 at p. 368:

> " 'Classes of insurants are expressly permitted but discrimination in favor of individuals in the same class and situation is prohibited. This gives the insurance companies power to make as many reasonable classes of insurants as the ingenuity of insurance managers may be able to suggest, so long as these classes are reasonable classes and do not by way of subterfuge or evasion create distinctions between individuals of one and the same class of insurants.' "

and then the comment is made concerning Ohio statutes:

> "It would seem that the Ohio statutes, while they prohibit discrimination between insurants of the same class, permit classification; that classification may be based on any reasonable difference; that there is a reasonable basis for a difference between the employees who pay upon the salary deduction plan and others who do not so pay; * * *"

It should be noted that the classification distinction which was upheld in this opinion was based upon a savings to the company in the loading factor such as the cost of collecting the premium. Your opinion request

indicates that the basis of the fees or rates that are to be charged each individual will be the hospital utilization of the "group" or "class" to which he belongs. Your requst also states that experience has demonstrated that there is actually a difference in hospital utilization by the employees of different employers. Some of the factors which might differ from employee group to employee group and which would bear on utilization are working conditions, frequency of physical examinations given the group by employers, extent of on the job medical aid, attitude toward use of hospitalization, length of time the employees have been covered by hospitalization, the economic level of persons within the group, the average age and sex of the group and the availability of hospital beds in the area.

Hospital utilization constitutes the peril or hazard involved in hospital service contracts and the differing experience constitutes a reasonable basis for a different rate. Past and prospective loss experience for the hazard insured against is an important factor in determining rates. See Sections 3937.02(A)(1), and 3935.03(C)(1), Revised Code.

Accordingly, in specific answer to your questions, it is my opinion and you are advised that hospital service association organized under Sections 1739.01 to 1739,15, Revised Code, may enter into group contracts so that the association is one contracting party and a "group," as a unit, the other contracting party, and that a hospital service association may base the fees it charges individuals on the hospitalization experience of the group to which the individual belongs.

Respectfully,
WILLIAM SAXBE
Attorney General